

Currencies: currently more pitfalls than opportunities

Everyone is bearish of the US dollar. If you agree, this ought to sound a few warnings for contrarian thinkers. Sure there are lots of reasons behind the dollar's fall, and just about everyone can rattle them off. These factors caused the Dollar Index to complete a two-year top in mid-2002, and subsequently fall 24.6 percent as of this month's low. For perspective, we should recall that the crowd was exceptionally bullish of the greenback, when the Dollar Index reached its peak in July 2001. While there is no technical evidence that the dollar's bear trend is over, it is currently oversold, near the 1998 and mid-2003 lows. These factors appear incapable of producing more than a temporary short-covering rally at present. However, as traders compete to see who can produce the most bearish forecast for the dollar, a greater force aims to prove them wrong.

The most powerful participants in foreign exchange - central banks - do not want the dollar to fall much further. First it was only the BoJ, which receives its intervention instructions from Japan's MoF. Then the ECB expressed concern about the euro's strength against the dollar in May and June, and again recently as those highs were tested. This month, the central banks of Thailand and South Korea have said they do not want their currencies to appreciate further. The market has noticed, judging from some short-term trend-stopping upward dynamics by the dollar against the strongest Asian currencies. South Africa's central bank is now responding to complaints over the rand's strength from mining companies and exporters, by slashing interest rates. Arguably, Alan Greenspan and John Snow lead the only central bank and treasury that do not oppose a weaker dollar. However, much of the Bush Administration's rhetoric concerning leaving currency levels to the market is likely to be electioneering.

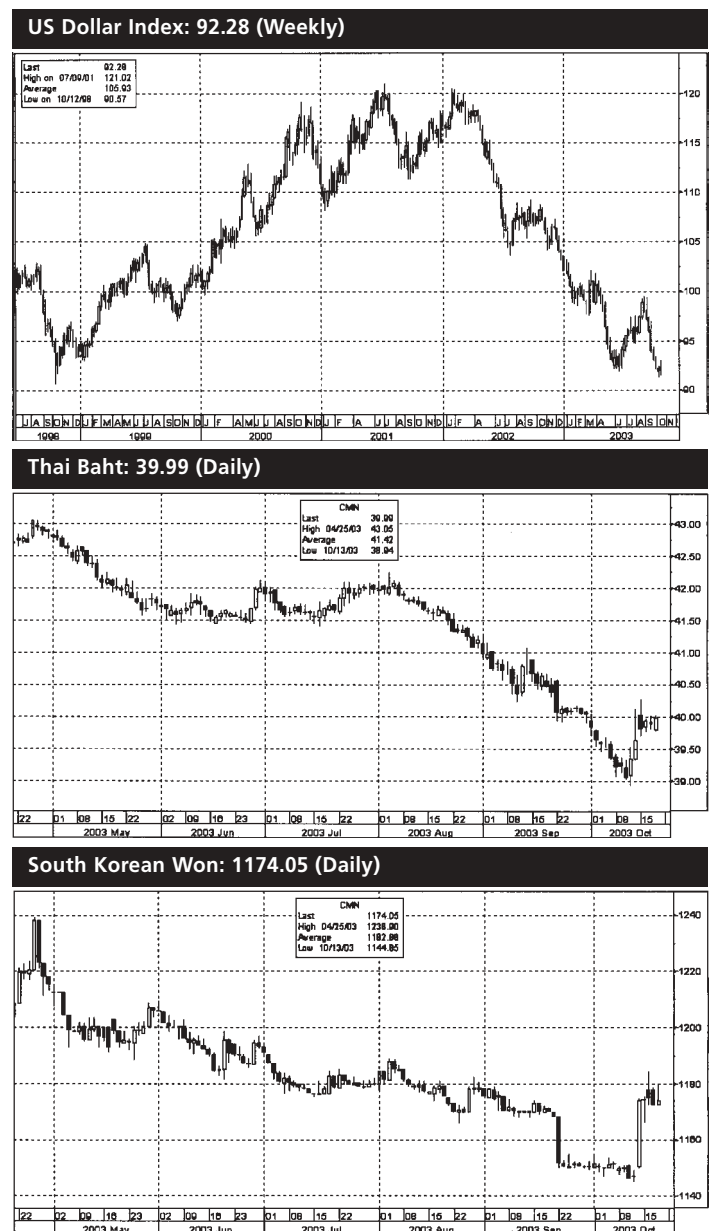
Conclusion - I am not saying that the US dollar has bottomed. However it shows some loss of downward momentum against most currencies and is likely to steady for a while, due to short covering. I maintain

that a dollar collapse is unlikely, not least because all of the important central banks would intervene, in their own interests.

I'll post charts of the US dollar against a number of other currencies on my website later today.

Best regards - David Fuller

Charts by Bloomberg



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